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SUBJECT: SPAIN: TELEFONICA'S VIEW OF VENEZUELA AND REST OF
LATIN AMERICA

¶1. DCM, accompanied by ECONOFF, met February 5 with Jose Maria Alvarez-Pallete Lopez, President of Telefonica International, to discuss Chavez's telcoms (e.g., CANTV) nationalization threats and their potential impact on Telefonica's Venezuela operations/investment. Alvarez-Pallete said that Telefonica was very concerned by Chavez's public remarks, but noted that it was still not clear what he actually intended to do. The details of Chavez's plans remain obscure (e.g., nationalization or expropriation, cell or just land lines, price to be paid) and until they were clarified, Telefonica could not assess their impact on its Venezuela operations/investment. To try to gain clarity, Alvarez-Pallete would fly to Caracas February 16. Alvarez-Pallete noted that Telefonica International enjoyed a good working relationship with Verizon International and that both were waiting for Telmex's offer for Verizon's stake in CANTV (if not rendered moot by Chavez's plans).

¶2. Alvarez-Pallete said that Telefonica's mobile phone operation was far more important than its seven percent stake in CANTV. He said that Telefonica was the largest of the three players in the Venezuelan cell phone market (40 percent market share) and was making money in the business. Telefonica's problem, however, was repatriating profits out of Venezuela.

¶3. Turning briefly to the rest of the continent, Alvarez-Pallete said that the alleged leftist drift of Latin America had been exaggerated and that Latin America at the end of 2006 enjoyed a better business climate than at the beginning of that year. He cited successful elections and stable business climates in Brazil and Mexico, as well as the stability of the Chilean, Peruvian and Central American markets. He argued that Venezuela, Bolivia and Ecuador were the exceptions, not the rule. He also stressed that Telefonica was making money in Argentina and was in the Argentine market for the long-haul, notwithstanding the

mercurial nature of the Argentine leadership.

¶4. Alvarez-Pallete said that Telefonica did business in every Latin American country with the exception of Paraguay, Bolivia and one other country whose name he could not recall.

He said that Telefonica participated in a group of 20-25 businesses that advised the Spanish political leadership with respect to Spain's Latin America policy. He noted that Telefonica was not in the U.S. market (except for a corporate office in Miami) and was still smarting from its 2000 purchase of Lycos just before the tech bubble busted (a operation in which he admitted that Telefonica "lost its shirt"). He did underscore, however, that 20-30 percent of Telefonica's stock was held by U.S. individuals and entities.

Asked for his views about U.S. policy in Latin America, Alvarez-Pallete encouraged U.S. business to stay in the region, noting that U.S. influence would decline if U.S. business abandoned the playing field.

Aguirre